Who Should Fix Resale Prices?[1]

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SHOULD the power to fix resale prices be lodged wholly with the manufacturer, or wholly with the dealer? This seems to state the problem of price maintenance as it is generally thought of in the present controversy. To deny the wisdom of both alternatives in the advocacy of a compromise between the two is the purpose of this paper.

The power of price maintenance is demanded only in connection with goods which are of the identifiable sort, and associated in their resale either with the name of the manufacturer, or with his trade-mark or brand. It would apply only to those commodities which are for the most part distributed through the conventional wholesale-retail channels. Within these limitations would be included probably more than half the volume of the country's retail trade. The majority of grocery commodities, excepting green goods, and the majority of drugs would be included, and smaller but nevertheless impressive proportions of ready made clothing, dress goods, toilet articles, shoes, hardware, jewelry, and novelties. In addition to virtually all of the country's specialty manufacturers, all the retail stores and wholesale houses are vitally concerned as is of course the entire body of the public.

Problem of Price Maintenance

Into this field of such wide and numerous interests, price maintenance has only recently entered as a problem of real importance. Its entrance may be explained as being due to a broadening of the functions of the manufacturers. They formerly were limited to producing commodities and transferring them to commission men or jobbers where they disappeared from sight and interest. Today we often find the manufacturer of specialties attempting to bring within his range of vision and influence not only the wholesale distributors, but also the retailers and ultimate consumers.

[1] This discussion is a fragment of a larger work by the author in Resale Price Maintenance now being issued by the Columbia University Press.

This broadening of function has been made possible by the vastly improved facilities and methods of advertising and transportation. In some cases it may be said that the manufacturer has reached that point where he combines within himself virtually all the functions of producer and salesman, even though he continues to make use of the jobbers and retailers.

This increasing control by the manufacturer over the destinies of the commodities which he produces has been facilitated by the agency of commodity standardization. The commodity is standardized in every conceivable way. Each unit is a perfect replica of every other unit. To these uniformities of quality, quantity, form, function and carton many manufacturers are adding price uniformity, maintaining that the efficacy of national advertising and the degree of public appreciation is thereby increased. It enables the manufacturer not only to emphasize various utilities, but also to emphasize attractiveness of price. Thus more effectually can a sense of real value be planted in the buyer. Undoubtedly to the great mass of the public there is a strong appeal in the one-price-to-all policy, especially so if there is present a conviction that the one price always commands the utilities desired. As the reputation of a standardized good increases, the price naturally becomes associated in the consumers' minds with the other characteristics which regularly identify the good.

It is asserted that when a commodity reaches this stage where its qualities and price are widely known and associated, it becomes especially subject to the evil of price cutting. The public, having associated for a long time a given commodity with a given price, will immediately detect a lowering of price and so confine their purchases of that commodity to the retailer who has cut the price. The effect is to compel competing retailers to meet the cut or else discontinue handling the commodity. In case there are any exceptions, they carry the good only as a necessary evil and handle it half-heartedly, preferring to offer substitutes where possible. Eventually the price cutters themselves, having exhausted the advertising value of the cut price, will lose interest in the commodity and either drop it or attempt to displace the demand for it by offering substitutes which afford bigger profits.

THE EVILS RESULTING FROM PRICE CUTTING

The evils which are said to result may be summarized as being: First, a decline in the value of the stock owned by dealers who are in the realm of influence exerted by the price cutters; second, a growing reluctance on the part of dealers to handle the commodity, their offering of substitutes, and a consequent decline in sales of the discounted commodity; third, losses suffered by the manufacturer and jobbers through the declining demand from retailers; fourth, inability of the public to secure conveniently the commodity of their choice, accompanied by the necessity of having to accept inferior substitutes.

To prevent price cutting, manufacturers resorted to many devices, the chief of which are: First, the manufacturer grants to such dealers as are willing to maintain the fixed price a liberal rebate on the list price, such rebate payable only when the goods are sold. Any variations from a fixed price entail forfeiture of the rebate. Second, many manufacturers have refused to sell at all to those dealers guilty of cutting prices below the standard. Some have gone so far as not only to refuse to sell to the offending dealer directly, but also to bring pressure to bear on all jobbers and retailers to refuse to supply the offender, thus making it impossible for the price cutter to renew his supplies from any source. Third, prices have been maintained by causing to be incorporated in the contracts of sale special provisions by which the dealers bound themselves to observe a fixed price. Fourth, by making conditional sales in which title to the goods sold to dealers remained in the manufacturer, and passed to the dealers only upon the completion of the resale made at the fixed price. The manufacturer reserved the right to demand the return of all unsold goods, upon the failure of the dealers at any time to maintain the price. Fifth, the use of a license agreement whereby the dealer is regarded merely as an agent or demonstrator without title in the goods. As agent he must sell at a stated price. His profits are in the form of commissions. Sixth, by affixing to the good or its container a statement to the effect that a certain price must be observed, the implication being that the use of such a notice made of the transaction a conditional sale, which bound the dealer to the fixed price. Seventh, a claim on the part of the manufacturer of patented or copyrighted goods

that the usual patent or copyright rights included the right to fix a resale price and to compel the observance thereof.

Virtually all these methods have in whole or in part been adjudged illegal by the supreme court, and in so far as they still exist, they are with very few exceptions merely nominal. Apparently no dependable price maintenance weapon is now available. Moral suasion is slightly efficacious, and the withholding of patronage from price cutters seems under certain very limited conditions to be legal. Yet this is by no means absolutely certain. It seems hopeless to expect the elimination of price cutting in the absence of special federal legislation to that effect.

THE STEVENS BILL AND RESALE PRICE CONTROL

Such legislation has been proposed in the form of the well-known Stevens Bill. Generally stated, its chief provisions are:

1. In any contract for the sale of trade-marked or branded goods the manufacturer may require the observance by dealers of a fixed price, provided that he has not a monopoly of the articles belonging to the same general class of merchandise, that his brand or trade-mark is registered with the Federal Trade Commission, together with the price lists, and that such contract permits a limited number of seasonal or disposal sales (two annually) in case the manufacturer does not choose to repurchase the goods himself on thirty days' notice from the dealer.
2. Emergency circumstances such as bankruptcy, fire, withdrawal from business, commodity deterioration, etc., may justify divergence from price only upon the approval of the manufacturer who demands thirty days' notice of such contemplated action, and who reserves the option to repurchase the goods in case he so desires.

The passage of this bill would clothe the manufacturer with unlimited power of resale price control. To his economic justification of this measure the manufacturer adds an ethical justification. It is argued that any given trade-marked commodity owes its existence to the enterprise and business ability of the producer. Upon it he expends his fortune, his energy, his business reputation. As the market is conquered, and as demand increases, the consumers begin to learn the manufacturer's name and trade-mark. The latter come to be associated with the commodity in the mind of the individual. In proportion to the number of individuals thus affected, the value of the trade-mark grows. It stands as an identification mark by which they may always recognize the

article and select it, rather than accept some competing commodity. If the good will value inhering in this trade-mark is the property exclusively of the manufacturer, and if price cutting by dealers constitutes an exploitation of this property, such an act must be looked upon as being ethically reprehensible.

The manufacturers are joined in their advocacy of the Stevens Bill by many dealers. They see in the device the advantage of greater stability in prices. Sharp price fluctuations eliminated, the perils of merchandising are largely diminished. Competition in that case would become a process involving service and efficiency rather than prices. With the standard price, selling is simplified, and profits are assured. Also the national advertising, financed by the manufacturer and thought to be dependent on the fixed price, is highly valued. Price maintenance would also diminish largely the fears entertained by the great mass of retailers of the growing power of the modern giants in retailing, the chains, department stores, and mail order houses. It is maintained that these largely owe their development, not essentially to economic superiority, but to their command over large capital united with their destructive policy of price cutting. Their price cutting is charged with being reprehensible in motive, being only for the purpose of deceiving the masses into the belief that their prices are uniformly lower than those of their competitors, whereas in fact their prices on unidentified commodities and on private brands which they push as substitutes are not only maintained but in many cases are actually excessive. Thus they recuperate from the losses on standard commodities, and at the same time injure the trade of the average retailers who can neither compete on the standard commodities nor afford to carry private brands.

PRICE CUTTING *v.* PRICE MAINTENANCE

Voices from among the consumers in behalf of price maintenance are not totally lacking. They emphasize the advantages to the consumers to be derived from standard commodities. The manufacturer freed from price cutting perils is in a position to offer better quality and is even enabled to enjoy economies which will encourage general and uniform price decreases. Furthermore they oppose the practice which imperils the life of commodities prized by the public.

The opponents of price maintenance make an issue of the truth of the above assertions and arguments. They deny that price cutting has the disastrous effects claimed, and assert that it is resorted to for the most part because of sound business reasons. As proof of this they are able to indicate numerous commodities, the popularity and distribution of which have rapidly increased rather than diminished despite their subjection to general and persistent price cutting. They attribute the disappearance of certain commodities from the market and the embarrassments of certain manufacturers, not to price cutting, but to inferiority of values offered, or to general inefficiency. They maintain that the existence of superior efficiency which is creative of economies in operating expenditures, and the presence of low cost conditions, constitute not only a valid defense of price cutting but also a moral insistence upon it.

To the claim that price cutting is an exploitation of the good will of the manufacturer, the opponents reply that they too have a good will which is based on a reputation for offering maximum values at minimum prices, and that to protect this good will they should not be prevented from passing to the consumer the benefits of economies achieved by them. They emphasize the fact that they own the goods which they sell, and that in their acquisition they paid the price which the manufacturer demanded. Why should the manufacturer who has received his price and who has given up title to the goods and responsibility in the goods be empowered to dictate to the present owners the conditions of resale?

Furthermore, the opponents of price maintenance profess to see in the use of the fixed price coupled with the enormous amount of advertising which it engenders an unwarranted encroachment on the legitimate functions of the retailer. The retailer is not a mere automaton engaged in the process of breaking up large quantities and distributing them in small units among a ready made clientele. He is a creator of utilities even as the manufacturer. Moreover recent phenomenal developments in merchandising would seem to demonstrate that it is no less responsive to applications of skill and judgment, art and science than is manufacturing. As regards capital expenditure, assumption of risk, and perplexing difficulties to be overcome, modern retailing

need not necessarily differ greatly from manufacturing. In no small number of cases these characteristics predominate on the side of the retailer.

Not only would price maintenance be an encroachment upon functions valuable to the public and involving vested interests of vast proportions, but it would bring the entire machinery of commodity distribution virtually within the control of the manufacturing end of industry, an obviously incongruous and dangerous development. The power to fix the resale price carries with it the power to fix dealers' profits. These would be raised or lowered not in accordance with dealers' interests but in harmony with those of the manufacturer. Concerted action on the part of manufacturers well entrenched behind a powerful consumers' demand created by intensive national advertising, could easily make of dealers' profits simply a form of wages, and in addition even dictate the methods and conditions of resale. The old American Tobacco Company methods are sometimes referred to.

The consumers opposing price maintenance would add to the above items the conviction that the fixed price would be tantamount to monopoly price, and that this would lead to a generally increased cost of living. This result would express itself in two ways: 1. Elimination of the present economies which are enjoyed through the patronizing of the cut price stores. 2. The establishment of conditions which would encourage the fixing of prices on a uniformly higher scale than now obtains.

The more one studies the irreconcilable arguments of the supporters and opponents of price maintenance, the more one is convinced that neither side is wholly wrong, nor yet wholly right. Impartial study of available data seems to justify the taking of a middle ground.

DEGREE OF CONTROL OVER RETAIL DISTRIBUTION

Is there economic justification for broadening the manufacturer's functions to include a degree of control over retail distribution where the manufacturer himself does not sell directly to the consumer? Obviously no such right arises from the consideration alone of the merits of his product or trade mark, because these receive their valuation and are paid for in the sale of the goods to the dealer. If such a right exists it must be sought for

not in the presence of certain qualities which the manufacturer has attached to his product, but in any service which the manufacturer may render in aiding the retailer to find a market.

Through different types of advertising such aid is often given. As regards most standardized commodities it is more effective and economical for the producer to advertise than for the dealer. A commodity of small unit value which no dealer could afford to advertise may easily justify the expenditure by the producer of hundreds of thousands in advertising. Equally evident is the fact that many commodities could never be manufactured profitably were it not for the large scale production made possible by wide advertising. These circumstances prevailing, it must be admitted that the manufacturer often rightly possesses an interest in retailing methods, but it does not follow that thereby the importance of the retailer is diminished. His functions have not been displaced or even restricted. They have only been supplemented.

The control then which the manufacturer has earned is one purely of degree. The true price maintenance problem is not "Should the manufacturer have the power of resale price control?" but "*To what extent* should the manufacturer have the power?" An answer indicating the minimum and maximum limits of this extent is, for practical purposes, sufficient.

We have noted that in many cases the manufacturer does actually share in the creation of the consumer demand. To be sure he profits from this. But so does the retailer. For the retailer then to take advantage of a mutually created situation to sell at a price which reacts injuriously upon the manufacturer would seem to constitute an act which the manufacturer should have the power to prevent. The question now becomes, "Does every price which is a cut price react injuriously upon the manufacturer?"

TYPES OF PRICE CUTTING

There are two quite distinct and totally different types of price cutting, the predatory type which for greater exactness we shall term "below cost" price cutting, and "profit yielding" price cutting. The former occurs where the dealer cuts to such a degree as to sacrifice all profits on the article cut. His purpose is to make good the loss by gaining increased patronage. The profit

yielding type occurs where the dealer either as a result of economies created by his own efficiency, or as a result of excessive gross profits allowed by the manufacturer is enabled to cut the price somewhat, but continues to make from it a fair profit. By far the greater part of price cutting is of this type. Nevertheless it has been condemned on the ground that it is only the first step in an epidemic of price cutting. But why should it become an epidemic? Why cannot the practice of price cutting be confined to that type called profit yielding?

Granting for a moment that this can be done, what would be the effect? It would amount to putting a premium on retailing efficiency, and encourage a general diminishing of prices in proportion to such efficiency,—a result highly to be desired by consumers. Among the price cutters themselves could appear no motive eventually to discontinue handling the good, and with respect to their competitors only the inefficient would be adversely affected. Losses to the manufacturer from their disaffection would be more than met by increased demands from the efficient. Yet it does not by any means follow that any given dealer by reason of modified price cutting privileges based on this principle could monopolize the sale of the discounted commodities in his community.

Taking an average competitive district under present conditions, we find the facts supporting this conclusion. On the city block where the author lives are three groceries carrying in general the same brands, but having totally different price schedules. One maintains prices fixed by the manufacturer; the other two cut prices but not uniformly. The maximum price store in this case does the biggest business, as it gives credit accommodations, makes deliveries, and has a selling force which knows how to please customers. Of the other two, one makes deliveries, but restricts its credit giving, and the third belongs to a chain whose slogan is "Cash and Carry." In these three stores prices vary as one would expect them to vary. Any well-known trade-marked food commodity which can be found in one can generally be found in the others. Yet a price variation in that particular commodity causes not the slightest dislocation in their respective businesses. How ludicrous it would be to insist on absolute uniformity of price in these stores, even though they are less than a stone's throw apart!

PREDATORY PRICE CUTTING SHOULD BE PROHIBITED

It seems safe to state that as a rule no evil can come to the manufacturer from price cutting provided it is not of the predatory type. The power to prohibit the latter should be granted, but with respect to the former no such power should be granted. Not only is it not needed for the manufacturer's protection, but it would lead to positive evils:

1. It would prevent the utilization of any means external to the manufacturer himself by which prices might be lowered. It ignores the various economic conditions in which different retailers are placed, and also the fact that retailers are not the same in business ability, nor are their business opportunities the same. It fails to take account of the varying costs of operation resulting from such dissimilarities. And reliable data prove that cost variation is not confined within narrow limits, but extremely wide ones,—from 10 per cent to 30 per cent.

2. With respect to service involved in retailing, the uniform price fails to take note that some stores are forced by their clientele to furnish prompt and expensive delivery service, are required to give expensive credit accommodations, and to provide costly and elaborate quarters and apparatus for the gratification of their customers. Obviously such stores should be allowed a higher price than the unpretentious establishment in poor and meagre quarters, affording no accommodation whatever, either by way of credit, or delivery, or floor service.

3. It fails to take note of the widely variant transportation charges which the goods have to meet. In the case of long distance transportation of heavy goods, the freight charges would constitute a very large item of expense. Price maintenance would compel all customers to bear the charge proportionally, regardless of their location, and as the territory of distribution widened, the price would come to include a virtual rebate to the more distant consumers at the expense of the others.

4. Unmodified price maintenance would tend to make more easy the attainment without economic justification of virtual monopoly on the part of manufacturers.

It is claimed that all specialty manufacturers would continue to meet competition, that the rivalry between brands and trademarks cannot be affected by price maintenance. "Why," say

they, "should competition between Ivory Soap and Fairy Soap be any the less with both subject to the fixed price?" The reply is that there is in price maintenance nothing inherently opposed to manufacturers' competition, but admission of this point does not refute the equally evident fact that price maintenance, while not preventing competition, does create conditions which discourage competition. Placing unquestioned responsibility on the manufacturer to fix not only his price to the jobber, but the price to the retailer and the consumer would so simplify the attainment of a combination or agreement that one of a most informal nature between two or three men would in many cases suffice for its realization. The motive for such an agreement between powerful competitors would be ever present. To place this motive within such easy reach of its incarnation would not in the long run be conducive to the best interests either of the public or of the majority of producers. Such a conviction is strengthened by the consideration that price maintenance has advantages only for the manufacturer whose commodity is already well established in the market, as the predatory price cutting is found only in connection with widely known goods. Paradoxical as it may seem, it is not only of value merely to the strong, but what is equally distinctive its value increases in a progressive ratio as the reputation of the producer increases. Price maintenance in the hands of an individual or a group dominant in the market by the power which it affords over retailing conditions gives to its owner an added advantage disproportionate to the justified economic advantage.

5. Further it must be objected that price maintenance donates to the manufacturers full powers over the distributors, but fails to provide for any material restriction of the manufacturers themselves. Not yet can it be said that all virtue resides in the manufacturers, and all vice in the dealers, nor can it be logically maintained that economic forces can be depended upon to govern the producers while the same forces fail utterly in the proper governance of the dealers.

6. One of the gravest objections to be brought against unmodified price maintenance is that it would tend to crystallize the distributive system and make practically impossible any changes that might lessen the cost of distribution. The present "spread"

between producer's cost and consumer's cost is too large. That fact is a matter of grave concern, and innovations aimed at its reduction should not be discouraged. Perhaps the chains, the mail order houses, the department stores, the coöperative associations, and the buying exchanges will contribute somewhat to the solution of the problem. Price maintenance aims a blow at all of them. It is difficult to see how it would fail to oppose every tendency toward transforming the present distributive system or reducing the costs thereof, unless such tendency emanated from the producers or especially favored their interests.

A modified form of price maintenance which is opposed only to the predatory type of price cutting, which permits price variations within the definite limits of cost variations, meets none of the above objections, and as has already been briefly indicated would be productive of positive benefits. It might be attained by placing in the hands of the manufacturer power legally to prohibit the cutting of prices below the margin which covers the cost of handling the commodity in question. A standard form of accounting should be prescribed for all dealers desirous of cutting prices. Upon properly authenticated cost data, periodical classifications of such dealers might be made and minimum schedules of prices arrived at for each class. Rough classifications should also be made of commodities based upon normal differences in rate of turnover, degree of perishability, susceptibility to seasonal demand variations, etc. To each class of dealers should be allotted a corresponding schedule of commodity classifications. In this way both the Scylla of rigid price maintenance and the Charybdis of predatory price cutting may be avoided.